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No.

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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1982

LOUIS N. RITTEN & CO.,

Petitioner,

v.

THE COMMISSIONER OF REVENUE,
STATE OF MINNESOTA,

Respondent.

SUPPLEMENTAL PETITION FOR A WRIT OF CERTIORARI TO THE MINNESOTA SUPREME COURT

MICHAEL J. MC ARDLE
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APPENDIX A

Opinion of the State of MINNESOTA TAX COURT dated April 22, 1981

STATE OF MINNESOTA

TAX COURT

Louis N. Ritten & Co., Inc.,	In the Matter of an Appeal from the Commissioner's Order dated October 2, 1979 Relating to corporation income tax liability for the taxable years 1972, 1973 and 1974.
Appellant,	
vs.	
The Commissioner of Revenue,	
Appellee.	Docket No. 3009
	Order Dated April 22, 1981.

The above entitled matter came on for hearing before the Honorable John Knapp, Judge of the Tax Court of the State of Minnesota, at 444 Lafayette Road, St. Paul, Minnesota, on May 14, 1980, beginning at approximately 10:00 a.m. With consent of respondent and permission from the Court, Henry M. Grannan, Esq., 20 N. Wacker, Chicago, Illinois, appeared for Appellant and Paul R. Kempainen, Special Assistant Attorney

General, appeared for Appellee.

This is an appeal from the order of the Commissioner of Revenue dated October 2, 1979, denying a claim for refund of excise taxes paid by the Appellant on interest from the United States government obligations for calendar years 1972, 1973 and 1974. The claims for refunds are in the amount of $15,958.26.

ISSUE

The issue is whether or not the business of the Appellant "consists exclusively of foreign commerce, inter-state commerce, or both" within the meaning of Minn. Statute § 290.03. Under that statute interest earned on investments in obligations of the United States are exempt from Minnesota income tax.

DECISION

The Appellant is not engaged

"exclusively" in inter-state commerce and is properly taxed under Minn. Statute § 290.02.

From the testimony adduced at the trial and from the files and records herein, the Court now makes the following:

FINDINGS OF FACT

1. The Appellant is a Minnesota corporation engaged primarily in the business of trading commodity futures, and investing the income therefrom. It is duly registered as a futures commission merchant with the U. S. Commodity Futures Trading Commission. The tax years at issue herein are 1972, 1973 and 1974.

2. The Appellant was incorporated under the laws of Minnesota in 1928. Until sometime in the 1960's, Appellant's sole offices were located

within the State of Minnesota, but in the 1960's offices were also opened up in Chicago. During each of the tax years in issue, the Appellant filed its state and federal income tax returns from its Minnesota office address at 109 Grain Exchange Building, Minneapolis, Minnesota.

3. At its Minneapolis office the Appellant employs six or seven employees; which includes the firm's Minneapolis brokers, three of the firm's officers (one of whom is also a broker), and a support staff. All of the Appellant's employees are licensed by the Commodity Futures Trading Commission and are governed thereby.

4. The mechanics of futures trading is outlined in an excerpt from the committee's report on H. R. 13113, which is appended to the committee print of the Commodity Futures Trading Commission Act

of 1974 on page 128 and 129. It reads as follows:

The Mechanics of Futures Trading

Placing Orders

The customer contacts a solicitor or account executive who in turn transmits the order, either directly or through a central office, to the exchange trading floor. The order is received on the trading floor by the firm's phone man. After recording and time-stamping the order, he gives it to a runner who carries the order to a floor broker in the designated trading area for that commodity. These trading areas are called pits or rings and each delivery month of a commodity is generally traded in a certain area of the pit or ring. Some firms no longer telephone orders to the floor. Instead, the orders are fed through a computerized system that transmits them to the floor via teletype.

Execution of Trades

The actual trading of futures contracts takes place in the noisy, boisterous setting of an auction-type market. The Commodity Exchange Act requires that all futures transactions in regulated commodities be executed on a commodity exchange designated by the Secretary of Agriculture as a "contract market."

Both the Commodity Exchange Act and the rules and regulations of the commodity exchanges require that futures transactions be executed openly in a competitive manner. Section 1.38 of the regulations under the Commodity Exchange Act reads as follows: "All purchases and sales of any commodity for future delivery on or subject to the rules of a contract market shall be executed openly and competitively by open outcry or posting of bids and offers or by other equally open and competitive methods, in the trading pit or ring or similar place provided by the contract market, during the regular hours prescribed by the contract market for the trading in such commodity." Certain carefully prescribed exceptions to competitive trading are allowed, but they do not nullify the general requirement of open and competitive trading.

The purpose of this requirement is to ensure that all trades are executed at competitive prices and that all trades are focused into the centralized marketplace to participate in the competitive determination of the price of futures contracts. This system also provides ready access to the market for all orders and results in a continuous flow of price information to the public.

The rules requiring competitive trading also require that all trades be executed in the area and during the hours designated by the contract market. Other exchanges can trade virtually identical contracts for the same commodity, provided they meet the requirements of a contract market as specified by the Commodity Exchange Act and are so designated by the Secretary of Agriculture.

Clearing Trades

After a trade has been executed, the confirmation of the trade retraces the path of the initial order within a few minutes. Final confirmation, however, cannot be made until the trade goes through the clearinghouse. In the clearinghouse, both sides of the trade must be matched, and any differences between the buyer and seller must be referred to the clearing firms involved for reconciliation.

A brief description of the clearing procedure for futures trading points out one of the major distinctions between futures and securities trading. Unlike securities, there is no certificate or document exchanged in a futures transaction. The futures contract is embodied in the rules and regulations of the contract market.

The clearinghouse (or clearing association) performs the functions of matching all buys and sells which are executed each day and of assuring the financial integrity of all futures transactions. As trades are matched and confirmed at the end of each trading session, the clearinghouse takes the opposite side of every transaction. It becomes the seller of all "buys" and the buyer of all "sells." Thus, when a trader establishes a position in the market, he does so with the clearinghouse, and when he offsets his position he offsets it with the clearinghouse. The clearinghouse assumes the legal responsibility for the opposite side of every transaction made on the contract market.

The clearinghouse requires that its members deposit margins to secure their firm's futures transactions. The clearing members, in turn, require margins from their customers. If the market moves against the open contracts of a clearing firm, that firm's initial margin is impaired and additional margin will be required.

Daily payments or receipts also occur between the clearinghouse and its members to account for daily price changes. The clearinghouse maintains the open accounts of member firms at the current market prices. At the

end of each day, these accounts are adjusted to the day's settlement price for each contract. Firms with net gains receive payment from the clearinghouse, while firms with net losses make payments to the clearinghouse. These receipts and payments of the clearinghouse exactly offset one another, with the clearinghouse merely transferring equity from losers to winners.

5. Pursuant to rules of the Commodity Futures Trading Commission, the Appellant is required, as a part of its business activities, to invest some of its customers' funds in federal government bonds and notes. This is not "another" business activity, but only an ancillary activity of its business. If the Appellant did not purchase the required securities, it would be in violation of the Commodity Futures Trading Act.

6. During the taxable year 1974 the Appellant maintained a savings account in its own name and using its own excess

funds at the Midland National Bank of Minneapolis, Minnesota. During 1974 this account earned interest for the Appellant in the amount of $63,243.00. Throughout the years in issue the Appellant also maintained other banking connections with the Midland National Bank of Minneapolis.

7. During each of the years in issue the Appellant invested segregated customer funds in its possession, which had been put up as margins to cover trades, in U.S. Treasury bills and bonds. The income realized from these transactions was duly reported by the Appellant on its income tax returns in the following amounts:

1972	$ 24,239.87
1973	$182,660.00
1974	$282,463.00

These U. S. Treasury bills and bonds were purchased by the Appellant through the Midland National Bank of Minneapolis as well

as through a Chicago bank. Those U. S. securities bought in Minnesota were kept in safe keeping at the Midland National Bank; and when they were eventually sold or turned in by the Appellant this was also done at the Midland National Bank in Minneapolis.

8. As mandated by regulations controlling the business activities of commodity brokers, the Appellant also invested in other marketable securities which were shown as assets on its balance sheets for each of the years in question, as follows:

Balance Sheet as of	Cost Value
12-31-72	$94,325.00
12-31-73	$76,725.00
12-31-74	$84,925.00

9. During each of the years in issue the Appellant also was required to own shares or memberships in the Minneapolis Grain Exchange Clearing Corporation, which were

treated as capital assets. As a result of this ownership, the Appellant received dividends from the Minneapolis Grain Exchange Clearing Corporation in the following amounts:

Year	Dividends
1972	$ 500.00
1973	$3,500.00
1974	$3,000.00

10. The Appellant originally filed its Minnesota Corporate Income Tax returns for each of the years in question on the basis that it was subject to the excise tax on corporations imposed by Minnesota Statutes § 290.02. On these returns, the Appellant included the interest income from its investments from U. S. securities.

11. On or about March 17, 1976, the Appellant filed claims for refund alleging that during the years in question it should have been subject to the net income tax on

corporations imposed by Minnesota Statute § 290.03, and that accordingly its interest income from U. S. securities was exempt from Minnesota taxation pursuant to Minnesota Statute § 290.08, subd. 8.

12. After administrative audit and review by the Department of Revenue, including a conference with Appellant's representative, the Commissioner issued his Order dated October 2, 1979, disallowing the claims for refund for each of the years in question. By his Order the Commissioner determined that the Appellant was a corporation "taxable under Section 290.02" and therefore not eligible to claim the exemptions set forth in subd. 8 of Minnesota Statute § 290.08.

CONCLUSIONS OF LAW

1. The Appellant is a domestic corporation subject to the normal excise tax imposed upon such corporations by Minn.

Statute § 290.02.

2. Appellant is not subject to taxation under Minn. Statute § 290.03, because its business within this state does not "consist exclusively of foreign commerce, inter-state commerce, or both."

3. As a corporation taxable under Minn. Statute § 290.02, Appellant's interest income from United States securities is subject to taxation by Minnesota pursuant to Minn. Statute § 290.08, subd. 13.

4. The Commissioner's Order herein dated October 2, 1979, is correct and proper and should be affirmed in all respects.

ORDER FOR JUDGMENT

The Order of the Commissioner of Revenue is hereby affirmed.

LET JUDGMENT BE ENTERED ACCORDINGLY. A STAY OF 15 DAYS IS HEREBY ORDERED.

MINNESOTA TAX COURT

John Knapp

John Knapp, Chief Judge

Dated: April 22, 1981.

EARL B. GUSTAFSON, Court Administrator of the Tax Court, State of Minnesota, does hereby certify that the attached instrument is a true and correct copy of the original on file and of record in my office.
Dated this 22nd day of April 1981
Barbara Skinner Deputy Clerk
Docket No. 3669

MEMORANDUM

Appellant acknowledges that it has a tax liability to the State of Minnesota. What is at issue in this case is: Under what section of Minnesota Statutes is the tax obligation computed? When Appellant originally filed its Minnesota tax return, it had computed its tax liability under § 290.02. This section imposes an excise tax on corporations. Upon review of the Minnesota tax law and regulations and applicable federal law, the Appellant decided that it should have been computing its Minnesota tax obligation under § 290.03 of the Minnesota Income Tax Act. Minnesota Statute § 290.03 is similar to § 290.02 except that it imposes an income tax instead of an excise tax, and under § 290.03 interest income from United States obligations is not taxed. Minnesota Statute § 290.03

applies to domestic corporations "which own property within the State or whose business in this State . . . consists exclusively of foreign commerce, inter-state commerce or both." Appellant contends that it complies with that statute.

The question is whether the Commissioner was correct in determining that the Appellant was taxable under Minn. Statute § 290.02. That statute read as follows for the taxable years at issue herein:

> 290.02 EXCISE TAX ON CORPORATIONS; IMPOSITION, MEASUREMENT. An annual excise tax is hereby imposed upon every domestic corporation, except those included within section 290.03, for the privilege of existing as a corporation during any part of its taxable year, and upon every foreign corporation, except those included within section 290.03, for the grant to it of the privilege of transacting or for the actual transaction by it of any local business within this state during any part of its taxable year, in corporate or organized form.
>
> The tax so imposed shall be measured by such corporations' taxable net income for the taxable year for which the tax

> is imposed, and computed in the manner and at the rates provided in this chapter. (Emphasis added.)

The Appellant clearly meets all the requirements for taxation under this statute. It is indisputably a domestic corporation which not only exists under the laws of Minnesota, but actively exercised its privilege of existence through the conduct of its brokerage business in this state during the taxable years in issue.

Appellant maintained its Minnesota offices at 109 Grain Exchange Building in Minneapolis, where it employed six or seven people, including brokers, three of the firms officers (one of whom is also a broker), and support staff.

During the years in question, Appellant also maintained a bank account for the investment of its excess funds at the Midland National Bank of Minneapolis,

Minnesota. Furthermore, Appellant bought and sold some of its United States securities entirely within Minnesota through the Midland National Bank, where the securities were also held for safekeeping.

Finally, but not unimportantly, it is quite obvious that Appellant's business at its Minneapolis office consists in large part of the receipt and acceptance of orders from Minnesota customers to buy or sell futures. These transactions do not take place on any exchange floor, but rather in or through the privacy of Appellant's Minneapolis office. These transactions are solely between Appellant and its own customers. As such, they take place totally within the State of Minnesota.

These facts clearly establish that Appellant is subject to the normal excise tax on domestic corporations imposed by Minn. Statute § 290.02. Therefore, its

interest income from United States securities is not tax exempt. The facts and the law in this case clearly show that Appellant's business operations do not come within the meaning of that statute's language requiring its business within Minnesota to consist "exclusively" of foreign or inter-state commerce.

Minn. Statute § 290.03, reads in relevant part as follows:

> 290.03 INCOME TAX; IMPOSITION, CLASSES OF TAXPAYERS. An annual tax for each taxable year, computed in the manner and at the rates hereinafter provided, is hereby imposed upon the taxable net income for such year of the following classes of taxpayers:
>
> (1) Domestic and foreign corporations not taxable under section 290.02 which own property within this state or whose business within this state during the taxable year consists exclusively of foreign commerce, interstate commerce, or both;
>
> Business within the state shall not be deemed to include transportation in interstate or foreign commerce, or both, by means of ships navigating within or

> through waters which are made international for navigation purposes by any treaty or agreement to which the United States is a party; (Emphasis added.)

There is no Minnesota case law on the meaning of the phrase "consists exclusively of foreign commerce, interstate commerce, or both" as used in this statute. However, the applicable Income Tax Regulations do set forth helpful guidelines as to the application of Minn. Statute § 290.03, especially as it relates to the normal excise tax on corporations imposed by Minn. Statute § 290.02. Regulation 2002 reads in relevant part as follows:

> The tax imposed by M.S.A. 290.02 is an excise or privilege tax measured for any given taxable year by the corporation's taxable net income for such year. The tax in the case of a domestic corporation is for the privilege of existing as a corporation during any part of a taxable year. . . . A domestic corporation is taxable under the provisions of M.S.A. 290.03 if its business within this State consists exclusively of interstate or foreign commerce or of both. Any corporation, foreign or

> domestic, whose business is partly interstate or foreign is subject to the excise tax, even though the predominant part of its business is not local. (Emphasis added.)

This regulation, duly promulgated many years ago pursuant to Minn. Statute §§ 290.52, makes it clear that if any part of a domestic corporation's business is local, it is subject to the excise tax imposed by § 290.02, rather than the net income tax imposed by § 290.03. In other words, even if it were assumed arguendo that a predominant part of a domestic corporation's business was interstate, this would still not meet the statutory requirement of "exclusively" interstate commerce.

In the case at hand, there is strong authority for the proposition that a corporation engaged in a business such as Appellant's, is in fact engaging in intrastate business, even though its business may also be considered to affect inter-

state commerce enough to give Congress the authority to regulate it under the Commerce Clause.

Federal regulation does not preclude state taxation and state taxation does not preclude federal regulation. Polish National Alliance vs. N.L.R.B., 322 U.S. 643, 649, 64S.CT. 1196, 1199.

In another case, both the Minnesota Supreme Court and the United States Supreme Court held that the business of a customhouse broker, licensed and regulated by the federal government for the purpose of easing the flow of foreign commerce across the Minnesota-Canadian border, was nevertheless sufficiently localized in nature to subject it to the provisions of Minnesota's Foreign Corporation Act. Union Brokerage Co. v. Jensen, 215 Minn. 207, 9 N.W. 2d 721 (1943); aff'd in 322 U.S. 202, 64 S. Ct. 967 (1944). In the U. S. Supreme

Court's opinion, 322 U.S. at 210, 64 S. Ct. at 972-973, it was said:

> But, as we have noted, while the business of Union is that of a custom-house broker, its activities are not confined to its services at the port of entry. It has localized its business, and to function effectively it must have a wide variety of dealings with the people in the community. The same considerations that justify the particular regulatory measure alone before us, namely the requirement of a certificate of authority in the case of foreign corporations carrying on business other than custom-house brokerage, apply to the carrying on of Union's business in Minnesota. The burden, such as it is, falls on foreign businesses that commingle with Minnesota people. (Emphasis added.)

The same can be said of Appellant in the case at hand. Despite the fact that it is regulated by the federal government, Appellant has also localized its business through a wide variety of dealings with the people of Minnesota. These include its receipt and acceptance of customer orders at its Minneapolis office. They also include its

maintenance of a bank account and other banking connections here, and mainly its maintenance of an office here in which three of the corporate officers are headquartered. All of these facts, together with its purchase and sale of U. S. securities entirely through a Minnesota bank with no part of the transactions being conducted over interstate lines, make it clear that at least a part of Appellant's business has been localized in Minnesota. Thus, its business within Minnesota does not consist "exclusively" of interstate commerce.

Appellant's citation of City of Waseca v. Braun, 206 Minn. 154, 288 N.W. 229 (1939), and several federal cases defining interstate commerce, are irrelevant. No one has denied that Appellant's business does in some measure affect interstate commerce. But this is not the test. Unless Appellant can show that it has no local business

whatsoever in Minnesota, and that its business within this state is "exclusively" interstate, then it is subject to the normal excise tax on domestic corporations imposed by Minn. Statute § 290.02.

Appellant's strong reliance upon the extensive federal regulation of the commodities futures business is likewise irrelevant. It is axiomatic that mere regulation of a business by the federal government under the Commerce Power, however pervasive, has little or no bearing upon the question of state taxation of that business. Braniff Airways v. Nebraska State Board of Equalization and Assessment, 347 U.S. 590, 594-597, 74 S. Ct. 757, 760-762 (1954).

This rule was highlighted in the case of Katzenbach v. McClung, 379 U.S. 294, 85 S. Ct. 377 (1964), where the U. S. Supreme

Court, in upholding the regulatory power of Congress to enact the Civil Rights Act of 1964, rejected as inapposite the citation of Commerce Clause cases dealing with state taxation. In 379 U.S. at p. 302, the Court said:

> Nor are the cases holding that interstate commerce ends when goods come to rest in the State of destination apposite here. That line of cases has been applied with reference to state taxation or regulation but not in the field of federal regulation.

It is quite obvious that the definition of interstate commerce found in the Commodity Exchange Act, 7 U.S.C. § 2, is not controlling in the instant case simply because it does not define what is "exclusive" interstate commerce for purposes of state taxation. In any event, the legislative history of the Commodity Futures Trading Commission Act of 1974 reiterates the fundamental purpose of the regulatory acts:

> " . . . insuring fair practice and honest dealing on the commodity exchanges and providing a measure of control over those forms of speculative activity which often demoralize the markets to the injury of producers, consumers, and the exchanges themselves." 1974 U.S. Code Congressional and Administrative News, p. 5844.

No portion of the federal act is intended to affect areas outside the scope of this statement of purpose. Thus, the federal preemption of regulation of this particular market does not also mean it preempts all state law that might apply to participants in the market. Poplar Grove Planting and Refining Co., Inc. v. Bache Halsey Stuart Inc., 465 F. Supp. 585 (M.D. La., 1979).

Appellant cites two Minnesota cases, Owens-Illinois Glass Company v. Commissioner of Taxation, Dkt. No. 196 (Sept. 24, 1946); and State v. Northwestern States Portland Cement Co., 250 Minn. 32, 84 N.W. 2d 373 (1957), aff'd in 358 U.S. 450, 79

S. Ct. 357 (1959), as "solid legal precedent" that Appellant too should be held a business engaged exclusively in interstate commerce. However, both of those cases are readily distinguishable from the instant case.

In both Owens-Illinois and Portland Cement, the taxpayers were foreign corporations who had never qualified to do business within Minnesota. Appellant, on the other hand, is a domestic Minnesota corporation which, by reason of that fact, has always had and exercised the privilege of doing business within this state. In fact, from the date of its incorporation in 1928, until sometime in the 1960's, Appellant's sole offices were located in Minnesota.

But the most important distinguishing factor between these cases is that in both Owens-Illinois and Portland Cement the

question of whether the taxpayer involved was engaged exclusively in interstate commerce was obviously conceded for the sole purpose of being able to proceed unhindered with the more important constitutional issues raised in those cases. Undoubtedly, one reason for this concession by the Commissioner was the very practical difficulty of establishing an intrastate business when neither the Owens-Illinois Glass Co., nor Northwestern States Portland Cement had even qualified to do business in Minnesota.

Another reason, quite evident in the Portland Cement case, was that the Commissioner simply wanted to test the constitutional validity of Minn. Statute § 290.03, as it applied to foreign corporations. Obviously, the Commissioner could not do so if he sought to tax Northwestern States Co. under the excise tax provisions

of Minn. Statute 290.02. This circumstance was noted by Justice Whittaker in his dissent to the opinion of the U. S. Supreme Court in Portland Cement. In 358 U.S. at 483-484, 79 S. Ct. at 371-372, Justice Whittaker reviewed the evidence in the case and said:

> These recitals, if found true, might very well have supported a finding, had there been one, that the taxpayer was engaged in intrastate commerce in Minnesota. Particularly might the statement about the salesmen taking orders from builders, contractors and architects for local dealers have done so, for it was expressly held in Cheney Brothers Co. v. Commonwealth of Massachusetts, 246 U.S. 147, 155, 38 S. Ct. 295, 297, 62 L.Ed. 632, that such conduct amounted to engaging in the local business of selling products for such dealers. But no such finding was made by the Minnesota courts. And there is more than colorable basis for believing that Minnesota did not desire such a finding, as any such practice could easily be ended by Northwestern, and Minnesota's purpose was not to rest on such a basis but to obtain an adjudication that its statute, § 290.03, constitutionally imposed a tax upon the taxpayer's net income from Minnesota customers though derived "exclusively

(from) interstate commerce."

The above points make it perfectly clear that neither Owens-Illinois nor Portland Cement amount to the "solid legal precedent" for which Appellant argues. In neither case was the question of what constitutes "exclusively" interstate commerce, within the meaning of Minn. Statute § 290.03, actually litigated. It was simply conceded by all parties. Furthermore, the Commissioner's allegedly inconsistent position as between those two cases and the one at hand is readily explainable upon the basis of different facts and different legal issues involved. In summary, Owens-Illinois and Portland Cement are of no help to the Appellant herein.